

PROBLEM 3-25 Break-Even Analysis; Pricing [LO 3-1, LO 3-4, LO 3-6]

Detmer Holdings AG of Zurich, Switzerland, has just introduced a new fashion watch for which the company is trying to find an optimal selling price. Marketing studies suggest that the company can increase sales by 5,000 units for each SFr2 per unit reduction in the selling price. (SFr2 denotes 2 Swiss francs.) The company's present selling price is SFr90 per unit, and variable expenses are SFr60 per unit. Fixed expenses are SFr840,000 per year. The present annual sales volume (at the SFr90 selling price) is 25,000 units.

Required:

1. What is the present yearly net operating income or loss?
2. What is the present break-even point in units and in Swiss franc sales?
3. Assuming that the marketing studies are correct, what is the *maximum* profit that the company can earn yearly? At how many units and at what selling price per unit would the company generate this profit?
4. What would be the break-even point in units and in Swiss franc sales using the selling price you determined in (3) above (i.e., the selling price at the level of maximum profits)? Why is this break-even point different from the break-even point you computed in (2) above?